

stock of another consenting corporation within any 6-month period beginning on a date on which a consent was filed under section 341(f)(1) by such other corporation. Section 341(f)(5) does not prevent a shareholder of a consenting corporation from receiving the benefit of section 341(f)(1) on the sale of additional shares of the stock of the same consenting corporation.

(i) [Reserved]

(j) *Special rule for stock ownership in other corporations*—(1) Section 341(f)(6) provides a special rule applicable to a consenting corporation which owns 5 percent or more in value of the outstanding stock of another corporation. In such a case, a consent filed by the consenting corporation shall not be valid with respect to a sale of its stock during the applicable 6-month period unless each corporation, 5 percent or more in value of the outstanding stock of which is owned by the consenting corporation on the date of such sale, file (within the 6-month period ending on the date of such sale) a valid consent under section 341(f)(1) with respect to sales of its own stock.

(2) The provisions of subparagraph (1) of this paragraph may be illustrated by the following example:

*Example:* Corporation X files a consent under section 341(f)(1) on November 1, 1965. On January 1, 1966, the date on which a shareholder of corporation X sells stock of X. X owns 80 percent in value of the outstanding stock of corporation Y. In order for the consent filed by corporation X to be valid with respect to the sale of its stock on January 1, 1966, corporation Y must have filed, during the 6-month period ending on January 1, 1966, a valid consent under section 341(f)(1) with respect to sales of its stock.

(3) For purposes of applying section 341(f)(4) (relating to the definition of a subsection (f) asset) to a corporation 5 percent or more in value of the outstanding stock of which is owned by the consenting corporation, a sale of stock of the consenting corporation to which section 341(f)(1) applies shall be treated as a sale of stock of such other corporation. Thus, in the example in subparagraph (2) of this paragraph, the subsection (f) assets of corporation Y would include property described in section 341(f)(4) owned by or held under an option by corporation Y on January 1, 1966.

(4) In the case of a chain of corporations connected by the 5-percent ownership requirement described in subparagraph (1) of this paragraph, rules similar to the rules described in subparagraphs (2) and (3) of this paragraph shall apply. Thus, in the example in subparagraph (2) of this paragraph, if corporation Y owned 5 percent or more of the stock of corporation Z on January 1, 1966, then Z must have filed a valid consent during the 6-month period ending January 1, 1966, in order for the consent filed by X to be valid with respect to the sale of its stock on January 1, 1966. In such case any of stock of either X or Y is treated as a sale of stock of Z for purposes of applying section 341(f)(4) to Z.

(5) If a corporation is a member of an affiliated group (as defined in section 1504(a)) that files a consolidated return, a corporation will be considered to have filed a consent if a consent is filed on its behalf by the common parent under § 1.1502-77(a).

(k) *Effective date.* Paragraphs (b), (c), (e)(3), and (f)(3) of this section apply only with respect to statements and notifications filed more than 30 days after July 6, 1977. Paragraph (d) applies only with respect to sales of stock made more than 30 days after July 6, 1977. All other provisions of this section apply with respect to transactions after August 22, 1964.

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#### DEFINITION

#### § 1.346-1 Partial liquidation.

(a) *General.* This section defines a partial liquidation. If amounts are distributed in partial liquidation such amounts are treated under section 331(a)(2) as received in part or full payment in exchange for the stock. A distribution is treated as in partial liquidation of a corporation if:

(1) The distribution is one of a series of distributions in redemption of all of the stock of the corporation pursuant to a plan of complete liquidation, or

(2) The distribution:

(i) Is not essentially equivalent to a dividend,

(ii) Is in redemption of a part of the stock of the corporation pursuant to a plan, and

(iii) Occurs within the taxable year in which the plan is adopted or within the succeeding taxable year.

An example of a distribution which will qualify as a partial liquidation under subparagraph (2) of this paragraph and section 346(a) is a distribution resulting from a genuine contraction of the corporate business such as the distribution of unused insurance proceeds recovered as a result of a fire which destroyed part of the business causing a cessation of a part of its activities. On the other hand, the distribution of funds attributable to a reserve for an expansion program which has been abandoned does not qualify as a partial liquidation within the meaning of section 346(a). A distribution to which section 355 applies (or so much of section 356 as relates to section 355) is not a distribution in partial liquidation within the meaning of section 346(a).

(b) *Special requirements on termination of business.* A distribution which occurs within the taxable year in which the plan is adopted or within the succeeding taxable year and which meets the requirements of subsection (b) of section 346 falls within paragraph (a)(2) of this section and within section 346(a)(2). The requirements which a distribution must meet to fall within subsection (b) of section 346 are:

(1) Such distribution is attributable to the corporation's ceasing to conduct, or consists of assets of, a trade or business which has been actively conducted throughout the five-year period immediately before the distribution, which trade or business was not acquired by the corporation within such period in a transaction in which gain or loss was recognized in whole or in part, and

(2) Immediately after such distribution by the corporation it is actively engaged in the conduct of a trade or business, which trade or business was actively conducted throughout the five-year period ending on the date of such distribution and was not acquired by the corporation within such period in a transaction in which gain or loss was recognized in whole or in part.

A distribution shall be treated as having been made in partial liquidation pursuant to section 346(b) if it consists of the proceeds of the sale of the assets of a trade or business which has been actively conducted for the five-year period and has been terminated, or if it is a distribution in kind of the assets of such a business, or if it is a distribution in kind of some of the assets of such a business and of the proceeds of the sale of the remainder of the assets of such a business. In general, a distribution which will qualify under section 346(b) may consist of, but is not limited to:

(i) Assets (other than inventory or property described in subdivision (ii) of this subparagraph) used in the trade or business throughout the five-year period immediately before the distribution (for this purpose an asset shall be considered used in the trade or business during the period of time the asset which it replaced was so used), or

(ii) Proceeds from the sale of assets described in subdivision (i) of this subparagraph, and, in addition,

(iii) The inventory of such trade or business or property held primarily for sale to customers in the ordinary course of business, if:

(a) The items constituting such inventory or such property were substantially similar to the items constituting such inventory or property during the five-year period immediately before the distribution, and

(b) The quantity of such items on the date of distribution was not substantially in excess of the quantity of similar items regularly on hand in the conduct of such business during such five-year period, or

(iv) Proceeds from the sale of inventory or property described in subdivision (iii) of this subparagraph, if such inventory or property is sold in bulk in the course of termination of such trade or business and if with respect to such inventory the conditions of subdivision (iii)(a) and (b) of this subparagraph would have been met had such inventory or property been distributed on the date of such sale.

(c) *Active conduct of a trade or business.* For the purpose of section 346(b)(1), a corporation shall be deemed to have actively conducted a trade or

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business immediately before the distribution, if:

(1) In the case of a business the assets of which have been distributed in kind, the business was operated by such corporation until the date of distribution, or

(2) In the case of a business the proceeds of the sale of the assets of which are distributed, such business was actively conducted until the date of sale and the proceeds of such sale were distributed as soon thereafter as reasonably possible.

The term *active conduct of a trade or business* shall have the same meaning in this section as in paragraph (c) of § 1.355-1.

**§ 1.346-2 Treatment of certain redemptions.**

If a distribution in a redemption of stock qualifies as a distribution in part or full payment in exchange for the stock under both section 302(a) and this section, then only this section shall be applicable. None of the limitations of section 302 shall be applicable to such redemption.

**§ 1.346-3 Effect of certain sales.**

The determination of whether assets sold in connection with a partial liquidation are sold by the distributing corporation or by the shareholder is a question of fact to be determined under the facts and circumstances of each case.

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CORPORATE ORGANIZATIONS

**§ 1.351-1 Transfer to corporation controlled by transferor.**

(a)(1) Section 351(a) provides, in general, for the nonrecognition of gain or loss upon the transfer by one or more persons of property to a corporation solely in exchange for stock or securities in such corporation, if immediately after the exchange, such person or persons are in control of the corporation to which the property was transferred. As used in section 351, the phrase "one or more persons" includes individuals, trusts, estates, partnerships, associations, companies, or cor-

porations (see section 7701(a)(1)). To be in control of the transferee corporation, such person or persons must own immediately after the transfer stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total number of shares of all other classes of stock of such corporation (see section 368(c)). In determining control under this section, the fact that any corporate transferor distributes part or all of the stock which it receives in the exchange to its shareholders shall not be taken into account. The phrase "immediately after the exchange" does not necessarily require simultaneous exchanges by two or more persons, but comprehends a situation where the rights of the parties have been previously defined and the execution of the agreement proceeds with an expedition consistent with orderly procedure. For purposes of this section—

(i) Stock or securities issued for services rendered or to be rendered to or for the benefit of the issuing corporation will not be treated as having been issued in return for property, and

(ii) Stock or securities issued for property which is of relatively small value in comparison to the value of the stock and securities already owned (or to be received for services) by the person who transferred such property, shall not be treated as having been issued in return for property if the primary purpose of the transfer is to qualify under this section the exchanges of property by other persons transferring property.

For the purpose of section 351, stock rights or stock warrants are not included in the term "stock or securities."

(2) The application of section 351(a) is illustrated by the following examples:

*Example 1.* C owns a patent right worth \$25,000 and D owns a manufacturing plant worth \$75,000. C and D organize the R Corporation with an authorized capital stock of \$100,000. C transfers his patent right to the R Corporation for \$25,000 of its stock and D transfers his plant to the new corporation for \$75,000 of its stock. No gain or loss to C or D is recognized.

*Example 2.* B owns certain real estate which cost him \$50,000 in 1930, but which has a fair market value of \$200,000 in 1955. He transfers